

STATEMENT OF SENATOR HOLLINGS
Hearing on the Airline Competition
July 27, 2000

Good morning. I want to thank the Chairman for holding this hearing. I also want to thank Mr. Klein and Dr. Kahn for agreeing to appear before the Committee today. Dr. Kahn, I know, had legitimate concerns about the air fares that almost prevented him from attending.

Let's start with one fact -- deregulation has not given us what we wanted, and the conditions it was supposed to rectify are worsening. When we passed the Airline Deregulation Act in 1978, we were promised a number of results -- low fares, better service, and the absence of predatory conduct (given that planes can easily be moved from one market to another). The government applied those theories to every transaction proposed, and with one exception, approved them all. The result is what we have today -- a balkanization of our aviation system --- 16 major hubs dominated by one carrier. New entry, real new entry is virtually unheard of, and people in small communities now have little choice in air fares (which are too high) or carriers. On top of all of this, we have carriers seeking to merge, creating further increases in industry concentration, and control over more fortress hubs, with virtually no promised relief for consumers.

The proposed United-US Airways merger is supposed to give us better, "seamless" travel. What it is likely to translate into, however, is a shift in revenues from one carrier to another--not better service, not lower fares. Even if the United-US Airways deal increases revenues 1-2%, it would result in \$300-\$600 in incremental revenues to the merged carrier. One analyst, Goldman Sach, indicated that "with fewer hub carriers, the airlines should become more disciplined in

capacity, marketing, and pricing plans. . . . [a] reduction in the number of network airlines creates a significant opportunity to raise connecting fares from medium to large spoke cities” We know what this means, and it is not good news for consumers.

Interestingly, Goldman Sachs acknowledges that investors are now conscious of the fact that airline mergers may “exacerbate service and labor woes”. That is precisely part of our problem here. Not only do we see further increases in concentration, but not surprisingly, we see less service. There are many risks associated with consolidation, including fortress hubs and the use of market power to keep out new entry.

Currently, there are at least 16 hubs where one carrier accounts for more than 50% of the traffic. This is where the market power resides. For years, we have heard that actual and potential competition would keep fares low, and in fact that is what the fathers of airline deregulation envisioned. I suspect that Dr. Kahn will tell us why we have not gotten what we were promised, but a large part of it has to do with the fact that every merger ever considered was approved by the government, facilitating fortress hubs. As one system grew bigger, other carriers had to respond with their own mergers. That is a trend we want to end.

Pick any hub today. GAO tells us that the hub carrier can effectively extract a fare premium. For example, US Airways today has almost 90% of the traffic at Charlotte, and the combined carrier would have 91%. The deal may give Charlotte better service, and more international connections, which I know are important to the people of Charlotte. What it does not do, though, is provide new competition for those that fly to and from Charlotte.

We are doing what we can in Congress to encourage new entry. In the recently enacted FAA bill, FAIR-21, we have proposed to direct DOT to cease funding of mega-fortresses, unless there is some assurance that the airports will make every effort to provide facilities for other carriers, and thus help address the market power concerns. The European Union is considering forcing major airlines to divest up to 5% of their slots at Europe's busiest airports to facilitate new entry. The EU, however, would go to a buy-sell system for slots. The U.S. did the same thing back in 1985, and it was a failure.

With respect to airports, and barriers to entry, we have asked GAO to give us information on the ability to get gates at some of the hubs. Gates are available at some hubs (Pittsburgh and Charlotte), but no one wants to challenge the incumbent carrier. At other airports we have heard that it is harder to get gates since the major incumbent may have a say in the use of gates at their respective airports. We have given the DOT the ability to stop that.

Mr. Klein and his office must continue to be active. They have challenged predatory actions by American, challenged the Northwest-Continental deal, and now must carefully consider not only the United-US Airways deal, but also the prospects that it will lead to additional deals. The DOT also must carry out its responsibilities, whether it is looking at competition policies, consumer policies or international deals. DOT has yet to issue a final set of predatory pricing guidelines. I know that the proposal was controversial, but it is time to address those concerns and issue the final rules.

In 1998, the Department of Justice challenged the Northwest-Continental deal based on an overlap of mere 7 markets affecting 4 million passengers. DOJ is well aware that we have untoward levels of market power -- which were granted or obtained in the name of efficiency -- which must be checked. The United-US Airways deal involves at least 4.9 million passengers in just the hub-to-hub routes of the two carriers, where there will a reduction from 2 carriers to 1, or from 3 to 2, depending upon the market. In many of those routes, there is no likely carrier able or willing to enter the market. Few times do we see a carrier, be it a low cost carrier or a network carrier, challenge routes connecting two hubs. With the feed traffic at each hub, the combined carrier effectively controls price, service and scheduling. In addition, several cities like Boston and New York will see significant increases in concentration, as will Dulles.

We will be back here next year looking at how best to address competition policy matters. We took the authority away from DOT in 1988, leaving it to our antitrust regulators. Next year, we will need to rethink that position. As it stands, we are going to be continuously beset by the types of problems we know exist, and will continue to exist, absent real competition and better service.

I look forward to the testimony of the witnesses.